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C O N F I D E N T I A L SECTION 01 OF 02 MOSCOW 000265

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TAGS: [EAIR](#) [ECON](#) [ETRD](#) [EINV](#) [RS](#)

SUBJECT: PUTIN SUPPORTS PLAN TO MERGE ROSTEKHNOLOGIA'S
AVIATION ASSETS INTO AEROFLOT

REF: A. A: MOSCOW 147

[B](#). B: MOSCOW 155

Classified By: ECONMINCOUNS Matthias Mitman for reasons 1.4 (b) and (d)

Summary

[1](#)1. (SBU) On February 2, Prime Minister Putin announced support for Transport Minister Levitin's plan to transfer Rostekhnologia's aviation assets to Aeroflot. According to Levitin's proposal, all the regional airlines that would have become Russia's new national carrier RosAvia, will be absorbed by Aeroflot. On January 26, in apparent anticipation of this decision, Aeroflot's board of directors approved the purchase of a 25.8% stake owned by private concern NRC (reftel B), enabling Levitin to engineer the transfer of those Aeroflot shares to Rostekhnologia in exchange for RosAvia's assets.

[1](#)2. (C) Despite the Putin announcement, Boeing continues to work with RosAvia's evaluation team on the tender to purchase up to 65 narrow bodied aircraft. According to a Boeing representative, RosAvia will present its assessment of the business offers to Rostekhnologia by the end of this week. Boeing also stated that the process of consolidating Rostekhnologia's aviation assets under Aeroflot will likely take at least a year. The tender is expected to be finalized over the short run but further delays are likely. End summary.

Terms of the Deal

[1](#)3. (SBU) On February 2, Prime Minister Putin's website reported that Putin fully endorsed Transport Minister Levitin's plan to transfer Rostekhnologia's aviation assets to Aeroflot. Levitin's proposal would transfer all the regional airlines that formed the basis of Russia's new national carrier RosAvia -- Rossiya, Orenburg, Vladivostok Air, Kavminvody, Saratov Airlines and Sakhalin Avia Airlines -- to Aeroflot.

[1](#)4. (SBU) The merger process will be complex, since some of the airlines are currently joint-stock companies (Vladivostok Air, Saratov Airlines and Sakhalin Avia Airlines) while the others are "federal unitary enterprises" (state-owned). Levitin's proposal is to engage the governor of St Petersburg in the process of preparing Rossiya, the largest carrier and the core of Rostekhnologia's aviation assets (reftel B), to become a joint-stock company before merging it with Aeroflot. Once all the airlines have become joint stock companies, Aeroflot and Rostekhnologia will jointly manage the group and eventually they will be merged with Aeroflot. According to

Levitin, as a result of this merger, Aeroflot would increase its share in the domestic market from 15% to 30-35% (which is compatible with the anti-monopoly regulations). Other details of the deal, such as the financial structure or the timeframe, have not been officially released.

Aeroflot Board Meeting Approves Share Purchase

15. (SBU) On January 26, Aeroflot's board of directors approved the purchase of a 25.8% stake in the company from NRC (reftel B). Reportedly, the price of the block (\$300-\$400 million) was 18-30% below its current market value and the purchase would be financed by a state-owned bank. The move reflects Levitin's plan to swap control over RosAvia for Aeroflot shares (according to media sources, only 10% of Aeroflot shares will be spent to get control over Rostekhnologia's assets). Industry analysts stated that Aeroflot will be 75% government owned versus the current 51% as a result of this deal.

Boeing continues negotiations

16. (C) Boeing representatives told us that they are continuing to work with the RosAvia evaluation team on the tender to purchase up to 65 passenger aircraft (reftel B). The assessment of the business offers will be presented to Rostekhnologia by the end of this week. Boeing officials stated that the process of consolidating Rostekhnologia's

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aviation assets under Aeroflot will likely take at least a year while the tender is expected to be finalized over the short run.

17. (C) Although RosAvia sources reportedly stated that the airline would likely cancel the aircraft purchase, Rostekhnologia officials told us that they "will continue with the tender anyway." However, as Deputy Prime Minister Shuvalov cautioned U/S Burns on January 14, price remains an issue -- with the possibility that Airbus could offer a lower price than Boeing (reftel A).

Comment

18. (C) Significant time and management effort will be required to consolidate all Rostekhnologia's aviation assets under Aeroflot, to integrate routes and unify the fleet. During this time, a decision on the tender likely will be delayed. The consolidation of Rostekhnologia's aviation assets into Aeroflot -- which in the past has favored Airbus over Boeing -- probably will significantly reduce Boeing's prospects for supplying the full quantity of aircraft tendered. End comment.
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